

BETWEEN THE CONTROL PERCENTAGE AND INTEREST PERCENTAGE IN ASSURING A FAIR IMAGE OF THE GROUP OF ENTITIES

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Abstract: At present, in Romania, the organizational-functional-juridical entity – the group of entity – perceived as an economical reality with an importance that competes with one of the individual entity, in the sense that we orientate our attention over the general acceptance adopted according to it “group capitalism” represents only another way to express the same economical truth.

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The establishment of a economic group entity, from the beginning based on the advantage of the existence of favorable juridical conjunctures and of some proper financial procedures and techniques, less vulnerable and more performing, is oriented towards a generous goal objective, the control of an ensemble of independent entities from juridical point of view and the placement of those under only one *unit decision*. The goal of achievement of this desideratum is to create a homogeneity in the realized activity, as well as the exceeding of the eventual disadvantages generated by the appearance of some outsized structures almost inherent in case of a company in a continue expansion.

At present, in Romania, the organizational-functional-juridical entity – the group of entity – perceived as an economical reality with an importance that competes with one of the individual entity, in the sense that we orientate our attention over the general acceptance adopted according to it “group capitalism” represents only another way to express the same economical truth. The groups of entities express in this way a more and more present reality in the Romanian contemporary business environment, and the processes to establish groups have a considerable amplex and reunite a varied scale of economical sectors where they act. The ascendant progressive trend is kept by the big industrial, commercial, banking groups (some times with an organizational and functional composite), quoted on exchange.

The existence of the decision unit at which the group notion responds involve a dependent upon relation between the coordination structure (group leader) and the other juridical entities of the group, dependence that has the following forms¹:

Dependence upon financial nature, that results by holding a majority of voting rights in the general shareholders gathering, this being able to be directly obtained, by

¹ V. Munteanu, A. Țurcan - Grupurile de societăți. Consolidarea contabilă, Ed. Economică, București, 1998.

holding more than 50% of voting rights, or indirectly, by interposing a juridical entity (or more) with an intermediary placement as right of control upon other entity.

Dependence upon managerial nature, that is assured by holding a majority in the administration council, managerial board, a.s.o., this dependence generating, for example, in the absence of manifested existence of an financial control, or the distribution of shares majority, or the agreement of a partner which does not want to assume administration responsibility.

Dependence upon contractual nature, which takes place by agreement with an associate entity (exclusiveness, succession or undertaking contract), or with some of its shareholders (agreement expressed by voting designation of administrators, a.s.o.)

Continuing on this line, we cannot omit the group entities building specific in case of Germany. This one is remarked by the existence and manifestation with success of the contractual dependence, very developed and with an extended application field (it can also be the result of the existence in the entity statute of some statutory clauses).

From the diversity of manifestation forms of between associate relations perspective, the group is, therefore, first of all an *economical reality* which primes upon the *juridical one*. This hypothesis finds its material expression in the facts that on legislative frame enacted in many European Union member countries, it does not recognize the juridical group personality.

The integration process of international concepts and norms of financial-accountant nature which vise the group of entity, especially the International Financial Report Standards (IFRS 3 particularly), presumes, at Romanian accountant referential level, an ensemble of mutations qualitative and quantitative nature with impact upon so-called integration.

Such mutations also vise the concepts of inclusion and exclusion from consolidation perimeter afferent to a group structure, fundamental concepts upon the methodology of determination and interpretation of **the percentages of control and interest**.

The determination of the exercised type of control creates the premises to establish the force reports that can be established between the group entities. To reflect the control nature it is necessary to recalculate the control percentage owned by the dominant entity, considering the dependence connection between this one and the other companies. The nature of dependence connections, direct or indirect, corresponds before all holding of voting rights which allow control exercise. In this sense, it is necessary the utilization of an instrument which allows power appreciation: **control percentage**.

This power appreciation must not be confused with financial dependence connection which results from holding a part of company capital, dependence which measures with help from another instrument called **interest percentage**.

To point out the role and the way in which those percentages find their utility in frame of consolidation process we will try a comparative approach of them, with underlining each of them specific.

Thus, while the control percentage represents the consolidating company capacity to control, directly or indirectly, a company susceptible to enter in consolidation perimeter, being calculate based on voting rights, without considering the

capital percentage (the quota of capital participation)², the interest percentage corresponds to the share that the mother company holds, directly or indirectly, in the capital of companies from the group. This one is an essential element to achieve the consolidation, because it stays at base of personal capital distribution and of the result between the mother company and shareholders (the interests pertaining to a minority).

Among the share companies, the titles (shares), indifferently that they are liberated or not, have in principle a voting right, but there are also exceptions, namely:

- Shares with prior dividends (preferential shares), without voting right
- Shares with multiple voting rights
- Shares with fractioned voting right

The total control percentage upon a company can be under 100%, of 100% (ordinary shares with simple voting right) or bigger than 100% (resulted by holding ordinary shares, with a single voting right, and nominative shares, with double voting right).

To determine the **control percentage** to totalize the control percentage hold, in a direct way, by the consolidating company and the control percentages hold by all companies which the consolidating company consolidates in an exclusive way. In exchange, the control percentages hold by the controlled companies in a subjunctive way or under a notable influence must not be retain³.

The control percentage finds its utility in determination of the consolidation method which can be applied.

In the international vision, we can notice a pronounced lack of convergence on the line of definition and utilization of consolidation methods.

Thus, the international referential defines three fundamental methods:

In the exclusive control case – the global integration method

In the subjunctive control case – the proportional integration method, as base processing (reference), or the put in equivalence method, as alternative processing (the other authorized processing)

In the notable influence case – putting into equivalence method.

According to the American standards US GAAP, the only consolidation method is global integration. The proportional integration is not admitted in accounts consolidation as, as a result, in case of participation associations (companies like “joint-venture”) on utilize the put in equivalence method. In a natural way, in case of associated companies, the put in equivalence method is not used as a consolidation method, but as an evaluation method.

Regarding the interest percentage, as a practical determination methodology, for each filiations, it multiplies the holding percentages (hold capital) of each company which constitutes the chain and it totalizes the percentages resulted from different multiplications, for each chain of the filiations.

In the same order of ideas, we consider that it is necessary to relate in detail the participation concept, surprised by hold rights in other companies’ capital point of view, materialized or not in titles which, by creating a durable connection with those, offers the possibility of decisional manifestation in issuing company.

² This one can be calculate by raport between the voting rights holded in a company and the total number of voting rights of this one.

³ E. Ropert – Nouvelle pratique de comptes consolides, Ed. Gualino, Paris, 2000, p.30.

In practice, there are find direct, indirect, mutual and crossing participations, those typology attracting entailing the necessity to present them in the explicative notes, together with a table of subsidiaries and participations. Thus, in the specialized literature⁴ got shape more aspects:

In case of direct participation, the control percentage is equal to the voting rights percentage of the mother company in one of its subsidiary.

Voting rights refer to the shareholders right with voting right. In this context, it must consider the shares without voting right which must be excluded from calculation, also the ones with double voting right which must be calculated.

The shares without voting right are specific to the companies that are foreseen with such situation in their statute and proceed from obligations conversion in usual shares, following the approval by shares holders. The number of shareholders without voting right cannot exceed 25% from social capital, according to the international practice.

Shares with double voting right are shares officially quoted held by stable company shareholders which have not give up their rights for at least 4-5 years.

The way we can calculate the shares with double voting right or without voting right can be exemplified like this⁵:

Case 1. A company M holds 40% of company A's shares, the only ones that have double voting right. The control percentage (Pc) of M company will be:

$$Pc = \frac{40\% + 40\%}{100\% + 40\%} = 50,7\%$$

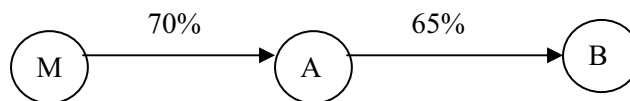
Case 2. A company M holds 75% of company A's shares, but a third of those are private from the voting right. The control percentage (Pc) of M company will be:

$$Pc = \frac{75\% - 25\%}{100\% - 25\%} = 66,6\%$$

In case of direct participation we can define two situations:

The existence of an unique chain, situation in which the control percentage is determined bearing after bearing, the chain being considered broken when a company is subjunctive controlled or is placed under a notable influence; the interest percentage presumes the multiplication of holding percentages (hold capital) of companies which form the chain.

For example, three entities, placed on a unique chain:

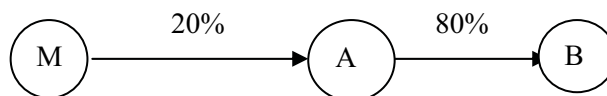


In this case, the mother company M holds, in a direct way, a control percentage of 70% in company A and indirectly in B a 65% percentage because it holds the exclusive control upon A and implicitly will also control B.

⁴ L. Malciu, N. Feleagă – Reglementare şi practici de consolidare a conturilor, Ed. CECCAR, Bucureşti, 2004, p.26.

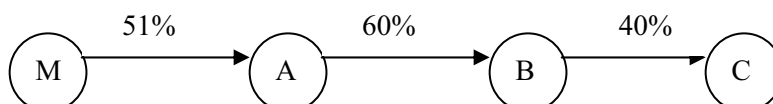
⁵ C. Iacob, D. Goagă – Contabilitatea societăţilor de grup, Ed. Sitech, Craiova, 2005, p.89.

If between the three entities presumed before we admit financial connections:



In this situation it appears a break in the chain because M company does not control in an exclusive way the A company. Therefore, the control percentage hold directly in A is of 20%, and indirectly in B is equal to zero.

Regarding the interest percentage, we presume that in the group companies, placed on a unique chain, there are the following connections:



To determine the interest percentage (Pi), it moderates in a successive way the hold percentages, from where it results:

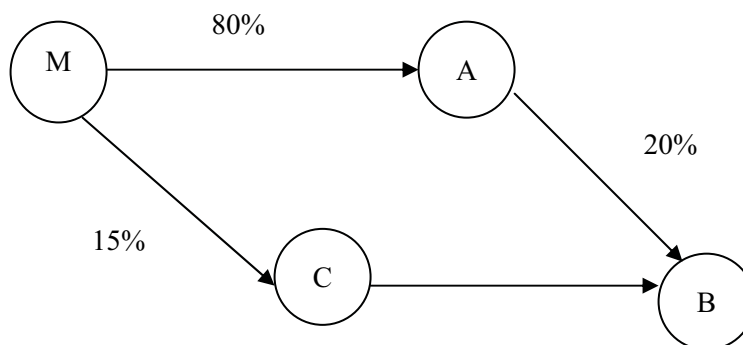
- Pi held by M In A is equal to the hold capital quota, 51%
- Pi held by M in B will be equal to $51\% \times 60\% = 30.6\%$
- Pi held by M in C will be equal to $51\% \times 60\% \times 40\% = 12.24\%$

Consequently, the participation percentage in a notion different from the control notion and represents the subordination connection or dependence between the mother company and group companies.

This way of calculation is specific only to direct subsidiaries, without chain breaking.

More chains existence, which presumes the control percentage determination by totaling the control percentages hold directly or indirectly for each of the companies which go before chain subsidiary, with pointing out the control break; interest percentage presumes that for each chain of the filiations it moderates the holding percentages (hold capital) of each company which constitutes the chain and to addition the results percentages for each filiations chain.

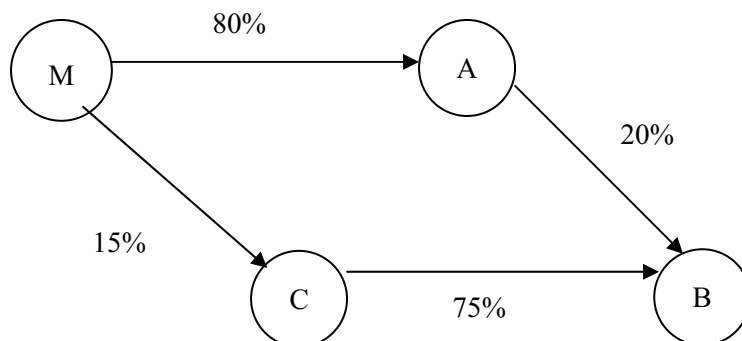
Let us presume a more complex connection between four companies, as follows:



In this case, company M exercises a direct control upon A of 80% proportion and upon C of 15% proportion. In comparison with C it should have the possibility to exercise a direct control through A or trough C. As it can be observed, through C

appears a break in the chain and, consequently the control percentage upon B is of only 20%.

To exemplify the way the interest percentage is determined, in this case, we will consider the following financial connections:



The interest percentage of M in A corresponds to the 80% participation quota, and in C of 15%. In comparison with B, company M has indirect connections, once through A and once through C, resulting the interest percentage is of $(80\% \times 20\%) + (15\% \times 75\%) = 27.25\%$.

The control percentage can be very important when the interest percentage is very low.

In case of complex participations

Such cases do not make the object of the regulations circumscribed in the perimeter of the International Accountancy Standards, being however presented in the evaluated countries accountancy, reason for which we consider opportune their reminder.

Through mutual connections: a share company cannot pose other company's shares if this one holds a fraction of it's capital, bigger than 10%, in lack of an accord between the companies interested to regularize the situation, the one which holds the lowest fraction from the other one's capital must lose it's investment⁶.

The calculation formula⁷ based on which we can determine the interest percentage in this case is:

$$\text{The interest of the group in B} = \frac{(1 - b) \times a}{1 - ab}$$

Where **a** and **b** represent the direct participation percentages.

To exemplify we consider that company M holds an 80% participation in company F's capital (IMF), and F holds a 10% participation in company M's capital (IFM).

The group interest in M, consequently the interest of stockholders in their company, M, will be:

⁶ L. Malciu, N. Feleagă – Reglementări şi practici de consolidare a conturilor, Editura CECCAR, Bucureşti, 2004, p.29.

⁷ Langlois G. şi colectiv – Comptabilite approfondie, Les editions Foucher, Paris, 1991.

$$IGM = \frac{1 - IMF}{1 - (IMF \times IFM)} = \frac{1 - 10\%}{1 - (80\% \times 10\%)} = \frac{0,90}{0,92} = 97,83\%$$

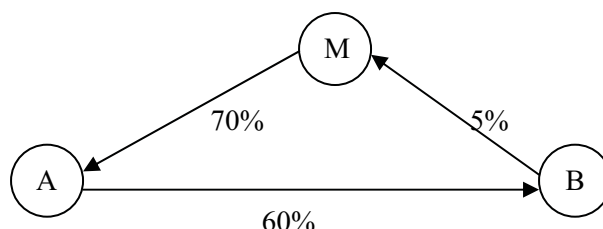
And the group interest in F company will be:

$$IGF = \frac{(1 - IMF) \times IFM}{1 - (IMF \times IFM)} = \frac{90\% \times 80\%}{1 - (80\% \times 10\%)} = 78\%$$

In France, a share company M is not allowed, according to the law, to possess shares in a company F, if company F holds a quota bigger than 10% in company M's capital.

We consider that there is a self control when a company holds a part of representative shares of its own capital through another company in which it holds directly or indirectly the control, what involves the voting right deprived of the self control shareholders.

Thus, we consider the following situation⁸:



We note:

IMA – the M interest in A 70%

IAB – the A interest in B 60%

IBM – the B interest in M 5%

IGM – the group interest percentage in M

IGA - the group interest percentage in A

IGB - the group interest percentage in B

As calculation formulas we generalize the formula applied in case of mutual participations.

$$IGM = \frac{1 - IBM}{1 - (IMA \times IAB \times IBM)} = \frac{1 - 5\%}{1 - (70\% \times 60\% \times 5\%)} = 97,03\%$$

$$IGA = \frac{(1 - IBM) \times IMA}{1 - (IMA \times IAB \times IBM)} = \frac{(1 - 5\%) \times 70\%}{1 - (70\% \times 60\% \times 5\%)} = 67,92\%$$

$$IGB = \frac{(1 - IBM) \times IMA \times IAB}{1 - (IMA \times IAB \times IBM)} = \frac{(1 - 5\%) \times 70\% \times 60\%}{1 - (70\% \times 60\% \times 5\%)} = 40,75\%$$

In case of crossing connections the reasoning has a superior complexity degree,

⁸ A. Tiron Tudor – Consolidarea conturilor, Ed. Tribuna Economică, București, 2000, p.54.

fact for which it is necessary, regarding the interest and control percentages determination, to use the matrix calculation and graph theory.

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